IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-753

INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHAUFFEURS, WAREHOUSEMEN AND HELPERS OF AMERICA,

Petitioner,

V.

JOHN DANIEL,

Respondent.

No. 77-754

LOCAL 705, INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHAUFFEURS, WAREHOUSEMEN AND HELPERS OF AMERICA, AND LOUIS F. PEICK,

Petitioners,

V.

JOHN DANIEL,

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ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

MOTION FOR LEAVE TO FILE AND BRIEF OF THE NATIONAL ASSOCIATION OF MANUFACTURERS, AS AMICUS CURIAE, IN SUPPORT OF THE PETITIONS FOR A WRIT OF CERTIORARI

NATIONAL ASSOCIATION OF MANUFACTURERS OF THE UNITED STATES OF AMERICA
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MOTION OF THE NATIONAL ASSOCIATION OF MANUFACTURERS OF THE UNITED STATES OF AMERICA FOR LEAVE TO FILE BRIEF AS AMICUS CURIAE IN SUPPORT OF THE PETITIONS FOR A WRIT OF CERTIORARI

The National Association of Manufacturers hereby respectfully moves for leave to file the accompanying brief as *amicus curiae* in this case. The consent of the Attorneys for the Petitioners has been obtained. The consent of the Attorney for the Respondent was requested but no reply was received.

The National Association of Manufacturers (NAM) is a non-profit voluntary business association, organized as a membership corporation under the laws of the State of New York. It is composed of over 12,500 manufacturing and related concerns, eighty percent of which have 500 or fewer employees, located throughout the United States. The NAM, therefore, represents a substantial number of the nation's industrial employers who employ, in the aggregate, over 16 million employees or roughly eighty-five percent of all employees employed in manufacturing nationwide.

A large number of the NAM's members have one or more retirement plans covering all or part of their work forces. Similarly, many of these plans are a by-product of the collective bargaining process. Because the decision below holds employee interests in such plans to be securities and thus subject to the antifraud provisions of the Securities Act of 1933 (15 U.S.C. § 77a, *et seq.*) and the Securities Exchange Act of 1934 (15 U.S.C. § 78a, *et seq.*) [hereinafter referred to collectively as the securities laws], and further because such plans are already extensively regulated by, *inter alia*, the Employee Retirement Income Security Act of 1974 (29 U.S.C. § 1001, *et seq.*) [hereinafter referred to as ERISA], many of the NAM's members will be directly affected by the decision in this case.

This case presents an issue of first impression concerning the applicability of the antifraud provisions of the securities laws to employee interests in retirement plans. The decision of the Seventh Circuit Court of Appeals instantaneously creates an enormous new class of potential securities law antifraud plaintiffs consisting of virtually all past and present participants in private retirement plans, and thereby exposes retirement trust funds and other parties to enormous, heretofore unanticipated,

potential liabilities. In addition to liability which may attach as a result of successful claims under the antifraud provisions, pension trust fund assets, as well as those of various other parties who, as a result of the decision below, are now subject to suit will be further eroded by the costs attendant to compliance with the affirmative disclosure requirements of the antifraud provisions, and the expenses which will naturally flow from the need to defend against even the most frivolous of claims for relief.

Moreover, the decision below has generated widespread uncertainty among those intimately involved in the formulation and administration of private plans with regard to their legal status and obligations under the securities laws. This confusion is exacerbated not only by decisions reached in other lower courts which conflict with the instant decision, but also by the fact that the decision below effectively negates certain policy decisions made by Congress and manifested in the various provisions of ERISA.

Recognizing that the provision of retirement security is completely voluntary, and because many pension plans are currently suffering severe financial hardship, it is not unreasonable to predict that the already high plan termination rate attributable, at least in part, to the enactment of ERISA will be accelerated by the holding below. Further, the decision below represents a significant disincentive to the adoption of new plans and the expansion of existing plans, and thus directly conflicts with the sound public policy favoring the continued growth and expansion of the nation's private retirement system.

Inasmuch as fair and adequate retirement income security enhances productivity through heightened morale, contributes to harmony in labor-management relations, and generally facilitates the realization of desirable social ends, the NAM has a legitimate interest in the proper resolution of the instant litigation. The views of NAM, its experience with the critical issues involved herein, and its general business expertise may be of

assistance to this Court.

Accordingly the NAM urges that leave be granted to file the accompanying brief as *amicus curiae* and respectfully so moves this Court.

Respectfully submitted,

NATIONAL ASSOCIATION OF MANUFACTURERS OF THE UNITED STATES OF AMERICA

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INTEREST OF AMICUS CURIAE

The interest of the National Association of Manufacturers in this case is set forth in the foregoing Motion for Leave to File Brief Amicus Curiae.

SUMMARY OF ARGUMENT

The holding below that an employee's mandatory noncontributory interest in a collectively bargained private retirement plan is a security which is acquired in a sale and is therefore subject to the major antifraud provisions of the securities laws raises important questions of first impression with regard to the proper scope of said laws. Because this decision gives rise to substantial costs and massive, heretofore unanticipated, potential liabilities and further has created widespread uncertainty with regard to the legal obligations of those involved in all aspects of private retirement plans, the continued viability and existence of the nation's private retirement system is seriously jeopardized. Accordingly, review by this Court to resolve the important issues raised herein is both warranted and necessary.

The lower court's finding of an investment contract, and thus a security, stems from its misapplication of the investment contract test which has emerged from this Court's decisions. The court's analysis is fataly flawed in that it ignores both common sense and the practical realities of the collective bargaining process, and distorts employment relationships beyond recognition. Thus, only by viewing the instant transaction completely out of its natural context is the lower court able to contruct an investment framework within which to force mandatory noncontributory employee interests in private pension plans.

Nor is the lower court's finding of a security supported by the legislative history of the securities laws. Rather, those portions of the legislative history relied upon below highlight Congress' failure to address the problems raised by the case at bar. Further, its interpretation of various portions of the legislative history gives rise to numerous questions which in themselves seriously undermine the heavy reliance placed on the legislative history by the lower court.

Assuming, *arguendo*, that pension interests of the type involved herein are securities, the court erred in finding the sale thereof in the instant context. The exercise of a voluntary choice related to the substance of the investment is a necessary prerequisite to the finding of a sale. No such voluntary choice exists in connection with mandatory noncontributory pension plan interests. The lower court thus errs in its strained attempts to find such a voluntary exercise in employment oriented, as opposed to investment related, decisions.

Policy considerations militate heavily against the soundness of the decision below. Because the lower court's holding instantaneously creates an enormous, largely uncontrollable, new class of plaintiff's under the antifraud provisions of the securities laws whose claims for relief will likely depend heavily upon hazy evidence of historical fact, the decision below flies directly in the face of past efforts by this Court to circumscribe the otherwise broad scope of the antifraud provisions. Potentially massive retroactive liabilities and expensive efforts to both defend against even the most frivolous of claims and to comply prospectively with the securities laws can be expected to result from the decision below and produce an enormous draining off of assets. This could completely frustrate the retirement expectations of plan participants who have complied with the requirements of their own plans. Similarly, the undefined nature of antifraud disclosure under the securities laws raises serious practical problems with regard to the content, form and timing of future disclosures. Finally, not only does the decision below effectively negate policy decisions made by Congress in other pension legislation, but any efforts to comply therewith by employers whose employees are represented by unions may well lead to unlawful disruptions of collective bargaining relationships and processes. Accordingly, the decision below should not be allowed to stand.

REASONS FOR GRANTING THE WRIT

The Court Below Erroneously Interpreted The Securities Laws By Making Them Applicable To An Employee's Interest In A Mandatory, Noncontributory Pension Plan Thereby Raising An Important Question Of Federal Law Which Has Not Been, But Should Be Settled By This Court

The decision below* holds: (1) that an employee's manda tory, noncontributory interest[1] in a collectively bargained defined benefit pension plan is an "investment contract", and thus a "security" within the meaning of the Securities Act of 1933, (15 U.S.C. § 77a, *et seq.*) [hereinafter "1933 Act"] and the Securities Exchange Act of 1934, (15 U.S.C. § 78a, *et seq.*) [hereinafter "1934 Act"]; (2) that a "sale" thereof for "value" takes place within the meaning of said Acts; and (3) that Section 17(a) of the 1933 Act (15 U.S.C. § 77q(a)), and Section 10b of the 1934 Act (15 U.S.C. § 78j(b)) and Rule 10b-5 thereunder, (17 C.F.R. § 240.10b-5), the major antifraud provisions of the securities laws, therefore apply to the transactions involved herein.

The decision below raises important questions of first impression with regard to both the proper scope of the securities laws and the extent to which the application thereof conflicts with, and thereby undermines, the nation's labor policy. If allowed to stand, the decision below could threaten the existence of many retirement plans as a result of massive, heretofore unanticipated, potential liabilities. Pension funds could also be seriously eroded by the costs attendant to compliance with, and litigation arising from, the regulatory requirements of yet another federal agency in an area extensively regulated under existing federal law.[2] Similarly, substantial confusion has already resulted among those involved in all aspects of pension plan formation and administration with regard to their legal status and obligations under this decision, a confusion exacerbated by contrary results reached in other cases.[3] Accordingly, we submit that resolution by this Court of the significant issues raised herein is both warranted and necessary.

* The decision below is reported at 561 F. 2d 1223 and is reprinted in full in the appendix to the instant Petitions for Writ of Certiorari. All references to the decision shall therefore be by citation to this appendix [hereinafter "App."].

[1] While used throughout our discussion, the term "interest" is used reluctantly. It is clear from the facts of this case that the plaintiff never acquired a vested interest, security or otherwise, in the subject pension plan and therefore never possessed a right to any benefits thereunder. Thus, his action herein is calculated to, in effect, create an enforceable interest where one has heretofore never existed.

a. The Court Below Misapplied the Test For Determining the Existence of an Investment Contract, and Thus a Security

The test for determining the existence of an investment contract within the purview of the securities laws originated in *SEC v. C.M. Joiner Leasing Corp.*, 320 U.S. 344 (1943), was later fully articulated in *SEC v. W.J. Howey*, 328 U.S. 293 (1946), and was recently reaffirmed in *United Housing Foundation Inc. v. Forman*, 421 U.S. 837 (1975). In these and other cases[4] this Court has considered the existence of an investment contract in varying factual contexts. These decisions make clear that individual components of a given transaction cannot be viewed in isolation. Rather, form must give way to substance, economic reality must be examined, and the transaction must be viewed in the context within which it arises to determine whether it is one of "the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits." *Howey*, 328 U.S. at 299; *Forman*, 421 U.S. at 849; *Tcherepnin v. Knight*, 389 U.S. 332, 336 (1967).

[2] The nation's private retirement system is currently subject to extensive regulation by the Department of Labor, the Internal Revenue Service, and the Pension Benefits Guarantee Corporation. *See generally* ERISA, 29 U.S.C. § 1001, *et seq.*

[3] Three District Courts have reached conclusions contrary to those reached below. *Hurn v. Retirement Fund Trust of the Plumbing, Heating and Piping Industry of Southern California*, 424 F. Supp. 80 (D.C.D. Cal. 1976); *Robinson v. United Mine Workers of America Health and Retirement Funds*, 435 F. Supp. 245 (D.D.C. 1977); *Weins v. International Brotherhood of Teamsters, Chauffeurs, Warehousemen and Helpers of America*, [1977] Fed. Sec. L. Rep. (CCH) ¶ 96,005 (D.C.D. Cal. March 28, 1977).

[4] *E.g.*, *Tcherepnin v. Knight*, 389 U.S. 332 (1967); *SEC v. United Benefit Life Insurance Company*, 387 U.S. 202 (1967).

The principal flaw in the lower court's application of the various elements of the investment contract test to the instant transaction is that its analysis necessarily assumes that a pension plan interest exists independently of the collective bargaining relationship from which it springs. Simply put, the court's narrow focus ignores the employment context within which the transaction exists. Once viewed in its proper context, however, factors fatal to the existence of an investment contract become readily apparent.

Here, unlike in the usual investment contract situation, the ultimate realization of benefits from the pension plan (*i.e.* the "investor's fortunes") is not critically dependent *solely* upon the efforts of others. Nor is this realization necessarily tied to that of other plan participants. Rather, the individual pension plan participant plays a significant role himself in determining whether he will ever receive retirement income. Thus, for example the investment success or failure of the pension trust fund, while certainly important, is largely academic if the employer is unable to continue making its contributions to the fund. The employer's ability to fund the plan in turn critically depends upon the continuing and consistent dedication, skill, and efficiency of each individual employee. Just as the trust fund is dependent upon the employer for its existence, so is the employer dependent upon employees for its continued economic viability and its consequent ability to fund the plan.

Similarly, the very fact that the pension plan is inextricably intertwined with the employment relationship dictates that here, in contradistinction to investments generally, the ultimate realization of benefits is subject to risks which are wholely unrelated to the investment success or failure of the fund itself and over which the individual participant has exclusive and complete control. Thus, an employee may never realize benefits from the plan if he quits his job, or if he loses his job as a result of misconduct or substandard performance. This vital interplay between the employment relationship and the pension interest, largely ignored by the court below, seriously undermines the finding of an investment contract for it further illustrates the significant control each plan participant has over his own receipt of future benefits.

Finally, those cases in which this Court has found an investment contract are marked by the presence of a deliberate decision on the part of an investor to part with his own money. Similarly, in those cases the predominant, if not the sole inducement for such action was the seller's favorable characterization of the investment attributes of the transaction.[5] In sharp contrast the transaction involved here is entry into or continuation of an employment relationship[6]. To find as the court did below that an employee makes an investment decision when he accepts employment, ratifies a collective bargaining agreement, or determines to continue in his job, perforce suggests that an expectation of profits from money invested through the pension plan is the predominant inducement for these deci-

[5] In *C.M. Joiner*, the investment character of the oil well drilling undertaking was widely advertised, 320 U.S. at 346; "[t]he exploration enterprise was woven into [the] leaseholds, in both an economic and legal sense [such that] the undertaking to drill a well [ran] through the entire transaction as the thread on which everybody's beads were strung." *Id.* at 348. Furthermore, it was clear that the economic interest in the well drilling undertaking was what brought into being the instruments being sold and which gave them "most of their value and *all of their lure*." *Id.* at 349, (emphasis added). In *Howey*, the investors were offered "an *opportunity* to contribute money and to share in the profits of a large citrus fruit enterprise managed and partly owned by [the seller]." 328 U.S. at 299. The investors were "attracted *solely* by the prospects of a return on their investment" and the transfer of land which accompanied the transaction was "purely incidental". *Id.* at 300 (emphasis added). In *Tcherepnin*, 389 U.S. at 333-4, the withdrawable capital shares were the entire substance of the transaction there involved and, as in *Joiner*, they were portrayed to potential purchases as desirable investments. See n. 8 *infra*, for a brief discussion of *SEC v. United Benefit Life Insurance Co., supra*.

[6] Significantly, to the extent that the lower court relies for any support on the fact that the decision to continue employment manifests an investment decision, it should be noted that the participant's status in this circumstance is no better than that of a shareholder who determines not to sell because of allged misrepresentations. As such, he has no standing to object under Section 10b of the 1934 Act or Rule 10b-5. *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S.723, 737-8 (1975).

sions. In other words, the lower court assumes that all of the myraid other factors which enter into a collective bargaining agreement or which bear on an employment decision (*e.g.* the nature of the job, wages, job security, or vacation time) are purely incidental to the pension plan interest. While an economy which affords one the luxury of making employment decisions on the sole basis of fringe benefits such as pension plans is perhaps desirable, it does not exist now and the court's analysis simply ignores this manifest reality.

In sum, to reach its result the court below has plucked the instant pension interest from its employment context and subjected it to fragmented analysis based on superficially appealing analogies. Common sense alone compels the conclusion that pension interests are incidental to, rather than determinative of, employment. Indeed, the SEC has itself so recognized.[7] To force such transactions into an investment framework simply ignores reality by examining pension interests in a vacuum as if they somehow have vitality independent of the relationships and processes from which they are born.[8]

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[7] In a memorandum to a Senate Subcommittee considering various proposals concerning the later enacted Welfare and Pension Plan Disclosure Act of 1958, the SEC stated:

> "many of these plans are the fruits of collective bargaining. *Accordingly, these plans are inseparably intertwined with labor management relations.* Abuses in this area then have their main effect upon an economic area in which the Commission does not possess expertise. (Emphasis added).

Hearings before the Subcomm. on Welfare and Pension Plans Legislation of the Senate Comm. on Labor and Public Welfare, 85th Cong., 1st Sess. 119 (1957).

[8] Neither *SEC v. Variable Annuity Life Insurance Company*, 350 U.S. 65 (1959) [hereinafter "*VALIC*"], nor *SEC v. United Benefit Life Insurance Company, supra,* weaken our conclusion that transactions must be viewed in their entirey with full recognition of the context in which they arise. In *VALIC*, the Court was not directly concerned with the presence or absence of an investment contract. Rather, the inquiry there was whether or not the security involved qualified for exemption from the registration requirements of the 1933 Act as an insurance contract. Thus, the Court assumed the existence of a security and attempted to distinguishing between different types of securities. *See generally Tcherepnin v. Knight*, 389 U.S. at 343-4. In *United Benefit*, before finding that the accumulation provisions of the contract involved therein constituted an investment contract, the Court first concluded that the "Flexible Fund" contract included two seperate and distinct promises whose operation was seperated at a fixed point in time. 387 U.S. at 207. Thus, there the two different features of the contract were found to have vitality independent of each other. *Id.* at 209. Furthermore, in neither *VALIC* nor *United Benefit* is the absence of a voluntary decision exclusively induced by the prospect of profit indicated.

b. The Legislative History Does Not Support the Lower Court's Finding of a Security.

The court below draws support for its conclusion that interests such as those here involved are securities from various portions of the legislative history supporting the securities laws. Looking primarily to a 1934 Senate amendment to the 1933 Act which was passed but then rejected in conference, and to changes in Sections 3(a)(2) of the 1933 Act and 3(a)(12) of the 1934 Act contained in the Investment Company Amendments Act of 1970, 84 Stat. 1413, the court concludes that Congress recognized mandatory, noncontributory employee interests to be "securities" within the purview of the securities laws. A careful reading of the portions relied upon, however, does not support such a conclusion.

The objective of the 1934 amendment, as stated by the lower court (App. 25), was to exempt from the registration requirements of the 1933 Act:

> an offering made solely *to employees of an issuer* (emphasis added) or of its affiliates in connection with *a bona fide plan for the payment of extra compensation* (emphasis by court) or stock investment plan for the exclusive benefit of such employees. 78 Cong. Rec. 8708 (1934).

One need look no farther than the above language, however, to conclude that interests of the type involved herein were not the target of this amendment.

Where the pension plan is operated throught a trust arrange-

ment[9], it is the trust itself which would be the "issuer" in an investment sense.[10] Similarly, the interest acquired by an employee is in the trust fund rather than in his employer's business. Thus, because the plan participant is not employed by the trust fund, the offering thereto of interests in the fund itself is not an offering made by an issuer to its employees.[11] Furthermore, the later comments of SEC Commissioner Purcell on the rejection of this amendment clearly suggest that only those plans wherein employees were given the opportunity to participate (*i.e.* voluntary plans) were affected.[12]

Nor do the 1970 amendments relied on by the court below further the inquiry into whether mandatory, noncontributory pension interests are securities. The court's finding in these amendments of a Congressional belief that such interests are securities stems, we submit, from the court's failure to distinguish between the relationship of the employees to the pension trust fund, and the fund itself as an investment medium.[13] We believe that the 1970 amendments focus on the latter while this case deals with the former. However, rather than repeat here the extensive and complex legislative history which we believe supports our conclusion, we simply note that the court's in-

[9] The pension trust in this case, as in all cases where a collective bargaining relationship is involved, was established pursuant to and maintained within the framework of Section 302(c) of the National Labor Relations Act of 1935, 29 U.S.C. §141, *et seq.;* 29 U.S.C. §186(c).

[10] 15 U.S.C. §77b(4); 15 U.S.C. §78c(a)(8); I L. Loss, Securities Regulation, 506-507 (2nd Ed. 1961); Mundheim and Henderson, *Applicability of the Federal Securities Laws to Pension and Profit Sharing Plans,* 29 Law and Contemp. Problems 795, 803, 813-814 (1964) [hereinafter "Mundheim and Henderson"].

[11] *See* H.R. Rep. No. 1838, 73rd Cong., 2d Sess. 41 (1934), wherein it is indicated that a basis for rejecting this proposed amendment was the "need [of plan participants for the] protection afforded by the availability of information concerning *the issuer for which they work . . .*". (Emphasis added).

[12] *Hearings on Proposed Amendments to the Securities Act of 1933 and the Securities and Exchange Act of 1934 before the House Comm. on Interstate and Foreign Commerce,* 77th Cong., 1st Sess. 895-6 (1941), [hereinafter "1941 Hearings"].

[13] *See generally* Mundheim and Henderson at 837.

terpretation raises several troublesome questions which undermine the significance attached to the amendments by the court.

The court reasons that the 1970 enactment amending Section 3(a)(2) of the 1933 Act (15 U.S.C. §77c(a)(2)) exempts employee interests in pension plans from the registration requirements of the 1933 Act[14] and thereby recognizes such interests to have been "securities" in the first instance. The court rejects the argument that these amendments do not focus on the employee's interest in the underlying pension plan by pointing to the "single or" language which precedes "collective trust fund maintained by a bank . . .". However, the "single or" language was not included in a concurrent amendment to the definition of "exempted securities" contained in Section 3(a)(12) of the 1934 Act (15 U.S.C. § 78c(a)(12)). H. Conf. Rep. No. 91-6131, 91st Cong., 2d Sess. 24-25 *reprinted in* [1970] U.S. CODE CONG. & AD. NEWS 1648, 1675-7.[15] There-

[14] The 1970 enactment added, *inter alia,* the following language to the "exempted securities" provision of the 1933 Act (15 U.S.C. §77c(a)(2)):

> any interest or participation in *a single or* collective trust fund maintained by a bank or in a separate account maintained by an insurance company which interest or participation is issued in connection with (A) a stock bonus, pension, or profit-sharing plan which meets the requirements for qualification under section 401 of Title 26, or (B) an annuity plan which meets the requirements for the deduction of the employer's contribution under section 404(a)(2) of Title 26, other than any plan described in clause (A) or (B) of this paragraph (i) the contributions under which are held in a single trust fund maintained by a bank or in a separate account maintained by an insurance company for a single employer and under which an amount in excess of the employer's contribution is allocated to the purchase of securities (other than interests or participations in the trust or separate account itself) issued by the employer or by any company directly or indirectly controlling, controlled by or under common control with the employer or (ii) which covers employees some or all of whom are employees within the meaning of section 401(c)(1) of Title 26. (Emphasis added).

[15] The court passes quickly over this anomaly by giving an explanation which suggests an interest conclusion (App. 28, n. 34). The court attributes this absence to the Commission's more limited interpretative and quazi-

fore, if the amendment to the 1933 Act encompasses an employee's interest in the underlying plan as the court suggests, and if such interests are indeed securities, then it would appear that the full range of regulatory requirements contained in the 1934 Act would become applicable since such interests would not then fall within the definition of "exempted securities under the 1934 Act.[16]

The court's interpretation thus raises serious questions with regard to whether the locations where these "securities" are "sold" to employees (*i.e.* the union halls and/or employer personnel offices) must either register or seek exemption from the requirement to register as an "exchange", (*see, e.g.*, 15 U.S.C. §§ 78c(a)(1), 78e, 78f); whether the nation's corporate personnel directors and union officials qualify as brokers or dealers and are thus subject to extensive regulation under the 1934 Act, (*see, e.g.*, 15 U.S.C. §§ *78c(a)(4), 78c(a)(5), 78o; 17 C.F.R.* § *240.10b-1, et seq.*);[17] and whether prior to the occur-

legislative powers under the 1933 Act in contrast to its plenary authority to exempt securities under the 1934 Act. Thus, we are asked to accept the questionable proposition that in simultaneously amending both pertinent provisions of the 1933 and 1934 Acts, Congress statutorily manifested its asserted intent in the 1933 Act, but was content to leave the realization of that same intent to administrative fiat under the 1934 Act.

[16] While it could be generally argued that the absence of a secondary market for employee interests in pension plans renders the 1934 Act, as a practical matter, inapplicable, the court below precluded such a conclusion by finding that "[e]ach year Daniel paid more value into the fund and from time to time plan amendments were effected which Daniel claims contributed to his being defrauded, [and that] [t]his is the conceptual predicate for finding a secondary distribution under Section 10b of the 1934 Act." (App. 41, n. 46).

[17] Significantly, since 1958 unions, union officials, and employers have been subject to extensive reporting requirements under the Labor Management Reporting and Disclosure Act, 29 U.S.C. § 401, *et seq.*, (1958). *See generally* 29 U.S.C. §§ 431-433. Employers were also subject to extensive additional reporting requirements under the Welfare and Pension Plan Disclosure Act, 29 U.S.C. §301, *et seq.*, (1958), *repealed* Section 111 of ERISA, 29 U.S.C. § 1031 (1974). Thus, it is unlikely that in 1970 Congress sought to impose additional complicated registration and regulatory requirements akin to those applicable to brokers and dealers under the 1934 Act without any explanation whatsoever. *See generally* 15 U.S.C. § 78o.

rence of a "sale" of such interests (*i.e.* prior to the hiring of new employees, the taking of ratification votes on agreements which contain changes affecting the pension plan, or prior to an employee's decision not to leave his job) the "security" must be registered under the 1934 Act, (15 U.S.C. §§ 78*l*, 78*l*(g)). We think it unlikely that Congress intended to trigger inquiries such as the foregoing with its 1970 amendments.[18] Nevertheless, the court below has now opened the door to widespread uncertainty by those who must deal with pension plans on all levels concerning their legal status and obligations under the securities laws.[19]

Finally, the legislative history supporting the 1970 amendments shows that Congress was not willing to permanently exempt interests or participations in "H.R.10" plans "because of their fairly complex nature as an equity investment and because of the likelihood that they could be sold to self-employed persons, unsophisticated in the securities field". H.R. Rep. No. 91-1382, 91st Cong., 2d Sess., 441 (1970); Staff of Senate Committee on Banking and Currency, 91st Cong., 2d Sess.,

[18] Needless to say, if we are correct in our belief that the 1970 amendments do not speak to the employee's interest in the underlying pension plan, but the court's conclusion that such interests are "securities" is upheld, then all of the requirements of the 1933 Act (*e.g.* registration under Section 5, 15 U.S.C. §77e) would apply absent an administrative ememption.

[19] Ironically, the 1970 amendments recognize the very distinction between employer contributions and employee contributions which the court below characterizes as "undue literalism" (App. 35). Since the net effect of the decision below is to transform what would otherwise be employer contributions into employee contributions, an interesting question is raised with regard to the resulting impact of this decision on the 1970 exemption. For example, since in the lower court's view there are no longer any "employer contributions", any amount expended by the fund to purchase securities issued by the employer would be "amount[s] in excess of the employer's contribution . . . allocated to purchase securities (other than interests or participations in the trust or separate account itself) issued by the employer . . . ". Thus, the result would appear to be that registration will now be required for all plans where contributions are held in a single trust fund maintained for a single employer, or in a separate account maintained by an insurance company, notwithstanding the clear intent of this provision to require the registration of such plans only where more than the employer's contributions are so used.

Analysis of S.34 at 1, 16 (Comm. Print 1969). In light of Congress' obvious concern for the "unsophisticated" self-employed purchaser of an "H.R.10" plan, its permanent exemption of employee interests in pension plans from the major disclosure provision of the 1933 Act, if the lower court's interpretation is correct, suggests the anomalous conclusion that the individual employee is more sophisticated in dealing with securities and thus did not need the protection of registration disclosure. We think it more reasonable to conclude that in amending the exemption provisions of the securities laws Congress was not focusing on individual employee interests, but rather on the activities of the pension fund itself in the capital markets.

c. The Lower Court Erred in Finding the Sale of a Security

Assuming, *arguendo*, that the lower court correctly found the participant's interest in the pension plan to be a security, the court clearly erred in finding that a sale thereof takes place in the instant context. Putting aside the questions of "disposition" and "value"[20], the court's erroneous finding of a sale derives from its dubious conclusion that volition is not required for a sale to take place, and is then compounded by its strained efforts to find, in the alternative, that volition is present here on the basis of occurrences and processes which are so remote from the substance of any supposed investment as to be virtually meaningless in an investment context.

Little need be said concerning the court's initial premise that volition is not a necessary prerequisite for a sale since it is based on little more than the absence of such an express requirement in the statutory definitions of sale. To attach any significance to this absence is to exalt form over substance and to indulge in precisely the type of unduly literal analysis decried by this Court in *United Housing Foundation, Inc. v. Forman*,

[20] Both the 1933 and 1934 Acts define "sale" in terms of the disposition of a security. 15 U.S.C. § 77b(3); 15 U.S.C. § 78c(a)(14). The 1933 Act additionally requires that the sale be for "value". 15 U.S.C. §77b(3).

supra. Rather, volition is the very essence of a security transaction[21] and has been specifically recognized as such by the SEC in the pension plan context.[22]

The court's strained efforts to alternatively find a voluntary choice are equally unpersuasive. One of the principal attributes of a noncontributory, mandatory pension plan is that the employee's coverage thereunder is automatic. The individual plan participant has no specific choice with regard to whether or not he will be covered by the plan and, as a practical matter, has little or no direct control over the terms and conditions of the plan, the level of benefits that will be paid, or the level of contributions that will be made by his employer.[23] In what sense then does the employee take any voluntary action which can be conceptualized as manifesting an investment decision?

For its answer the court looks beyond the substantive boundaries of the supposed investment to infer an investment

[21] Our conclusion that the exercise of an individual voluntary choice related directly to the substance of the investment is a necessary prerequisite to the existence of a sale is not affected by the cases relied on below (App. 36). In *Vine v. Beneficial Finance Co.*, 374 F.2d 627 (2d Cir. 1967), *cert. denied*, 389 U.S. 970 (1967), the question was not the buyer's standing to complain, but rather that of the "forced seller". Significantly, there the "forced seller" did have an individual choice to either abide by the merger or cash in his stock. Similarly, in both *Zeller v. Bogue Electric Manufacturing Corp.*, *476 F.2d 795 (2d Cir. 1974), cert. denied*, 414 U.S. 908 (1973), and *International Controls Corp. v. Vesco* 490 F.2d 1334 (2d Cir. 1974), *cert. denied*, 417 U.S. 932 (1974), a voluntary choice relating to the substance of the investment existed, but its exercise was controlled. These situations are dramatically different from the case at bar wherein the absence of a choice *ab initio* is inherent in the transaction itself rather than artificially imposed by collateral circumstances such as ownership of controlling interests.

[22] See n. 28, *infra*. Significantly, the SEC's change in position is apparently based not on the absence of volition as a requirement of sale, but rather on its efforts to find the requisite volition in other quarters. (App. 37-38).

[23] Generally, these are decisions made by the plan trustees or by the employer and the union during negotiations. To the extent that these considerations are negotiated and dealt with in the collective bargaining process, it is the union, as the employees' legally recognized exclusive representative which has wide discretionary authority over such determinations. *See generally Vaca v. Sipes*, 386 U.S. 171 (1967).

decision from the union members' choice to either ratify collective bargaining agreements which contain the pension plan and subsequent agreements governing the level of employer contributions, or to seek the dismissal of union officers or union decertification. (App. 35-36). The court finds additional volition in the employees' decision to retain his job. *Id.* However, the requisite volition can certainly not lie in any type of ratification procedure[24] for this would result in the creation of an arbitrary distinction between plans covering unions that have ratification procedures and those that do not.[25] The only remaining possibilities are the decision to accept employment and the decision to continue employment. While these may qualify as individual voluntary choices, they do not necessarily have anything to do with the supposed investment and simply defy conceptualization as the type of decisions which Congress sought to facilitate when it ". . . substitute [d] a policy of full disclosure for the philosophy of *caveat emptor.*" *Santa Fe Industries, Inc. v. Green,* 45 U.S.L.W. 4317, 4321 (1977); *SEC v. Capital Gains Research Bureau,* 375 U.S. 180, 186 (1963).

[24] In its discussion, the court draws a rather unusual analogy, the meaning of which is not entirely clear, to corporate mergers. (App. 36). To the extent, however, that the court is suggesting that individual volition exists despite the fact that the decision reached by the collective is contrary to that individual's wishes, the analogy is inapt. SEC Rule 133, 17 C.F.R. § 230.133, *rescinded* 37 Fed. Reg. 23636 (1972), the basis for the Commission's "no sale" position in the merger context was rescinded in recognition of the fact that each shareholder did indeed have an individual choice. Thus, in rescinding the rule, the Commission stated: "In voting, each consenting stockholder is expressing his voluntary and indivudal acceptance of the new security, *and generally the disapproving stockholder is deferring his decision as to whether to accept the new security or, if he exercises his dissenters rights, a cash payment.*" SEC Securities Act Release No. 5246 at 3 (1972) (emphasis added). There is no analogy to the dissenter's right of appraisal in the instant context. If the employee does not meet the eligibility requirements, he forfeits his benefits. He cannot simply cash in his unvested benefits.

[25] Unions are not required to seek member ratification unless their own constitutions or by-laws so require. *See, e.g., International Union of United Automobile, Aircraft and Agricultural Implement Workers of America v. O'Brien,* 339 U.S. 454 (1950); *NLRB v. Borg-Warner Corp.,* 356 U.S. 342 (1958); *Cleveland Orchestra Committee v. Cleveland Federation of Musicians,* 303 F.2d 229 (6th Cir. 1962).

d. Policy Considerations Weigh Heavily Against the Soundness of the Result Reached Below

In *Blue Chip Stamps v. Manor Drug Stores, Inc.* 421 U.S. at 737-749, this Court recognized the significant role played by sound policy considerations in defining the contours of private action under the antifraud provisions of the securities laws. Of principal concern to the Court were the undesirable consequences of rendering a decision which would create a largely uncontrollable expansion of the class of potential plaintiffs under the antifraud provisions. Notwithstanding the fact that potential investors who had suffered actual damage would be denied redress by its ruling, the Court was persuaded that the possibility of vexatious litigation counseled against opening the courts to claims for relief by those who had neither purchased nor sold a security.[26] In this the Court was primarily concerned with the potential settlement value of "strike suits" and the likelihood that a contrary ruling would "throw open to the trier of facts many rather hazy issues of historical fact the proof of which depend[s] almost entirely on oral testimony." 421 U.S. at 743.

These same considerations, as well as others, seriously challenge the soundness of the decision below. For example, the decision below instantaneously creates a cause of action in favor of virtually every past and present private plan participant.[27] Plans of the type involved herein have for years been

[26] This decision is but one in a series of recent decisions wherein this Court has attempted to circumscribe the otherwise broad scope of the securities laws. *See, e.g., Santa Fe Industries, Inc. v. Green, supra; Ernst & Ernst v. Hochfelder,* 435 U.S. 185 (1976); *United Housing Foundation, Inc. v. Forman,* 421 U.S. 837 (1975); *Blue Chip Stamps v. Manor Drug Stores,* 421 U.S. 723 (1975). *See generally* Lowenfels, *Recent Supreme Court Decisions Under the Federal Securities Laws: The Pendulum Swings,* 65 Geo. L.J. 891 (1977).

[27] This new class of plantiffs is not limited to participants in collectively bargained, mandatory, noncontributory plans. Under the reasoning employed by the court below, distinctions between different types of plans no longer exist for purposes of the securities laws.

operated without reference to the securities laws because, until this decision, "no court had ever held, nor apparently had anyone including the SEC the temerity to argue that an interest in an involuntary, noncontributory pension or health benefit plan was covered by the securities laws." *Robinson v. United Mine Workers of America Health and Retirement Fund,* 435 F. Supp. 245, 247 (D.D.C. 1977) (footnote omitted).[28] Thus, it is reasonable to assume that few if any employers, unions, or plan administrators have made disclosures sufficient to meet antifraud standards. To borrow the lower court's own figures then, roughly 30 million current and an indeterminant number of past plan participants can now sue for breach of the antifraud provisions.[29] (App. 24) Additionally, affording a legal remedy to those who have failed to meet the eligibility requirements will inevitably open the door to much litigation the primary focus of which will be "hazy evidence of historical fact" concerning the source and content of representations made years earlier to plan participants. Thus, both of the fears expressed

[28] Through the dubious medium of an *amicus* brief filed below, the SEC seeks to reverse its early position that "no sale" occurs in connection with mandatory, noncontributory plans. Opinion of the Assistant General Counsel of SEC (1941), ['41-'44 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 75,195 *reprinted in* [1977] Fed. Sec. L. Rep. (CCH) ¶2105.53; Testimony of Commissioner Purcell, 1941 Hearings at 896-897; Mundheim and Henderson at 807-812. While the Commission vigorously asserts in this case that the "no sale" rationale was applied only in the registration context and has never been, and should not now be, extended to the antifraud provisions, for aught that appears (App. 52), the Commission has never actively applied the antifraud provisions to such plans. Nor, given the underpinnings of its rationale (*e.g.* the absence of value and/or volition), would anyone ever reasonably suspect that the antifraud provisions applied.

[29] The creation of this enormous new class of plaintiffs portends massive, heretofore unexpected, potential liability for employers, unions, and pension trust funds alike resulting from successful claims under the securities laws as well as for legal fees and other costs attendant to both successful and unsuccessful suits. Additional costs will, of course, be incurred to affirmatively comply with the disclosure requirements now found to be applicable. In the final analysis, however, those who will suffer the most harm are the plan participants who have met or will meet their eligibility requirements only to find that their retirement funds have been severely depleted by the "costs" of the decision below.

by this Court in *Blue Chip Stamp* may well become a reality if the decision below is not overturned.

Massive retroactive liability and the inherent unfairness of evaluating transactions completed years earlier against present-day standards are not, however, the only serious practical consequences of the decision below. Prospective compliance with the antifraud provisions and the disruptive impact thereof on labor-management relations also give rise to serious concerns. Chief among these is the fact that the decision below effectively renders superfluous various provisions of Title I of ERISA, (29 U.S.C. §§1001-1144), and reverses certain clear policy decisions which were made by Congress and manifested in ERISA.

With regard to reporting and disclosure, ERISA represents a conscious focusing of Congressional attention on the informational needs of employees *qua* pension plan participants Thus, in §§ 101(a), and 102(a)(1) of ERISA, Congress required distribution to plan participants of summary plan descriptions which "shall be written in a manner calculated to be understood by the average plan participant and which shall be sufficiently accurate and comprehensive to reasonably apprise such participants and beneficiaries of their rights and obligations under the plan." 29 U.S.C. §§ 1021, 1022. Similarly, Congress determined what information was "material" in this context and specified in §102(b), (29 U.S.C. § 1022(b)), precisely what information summary plan descriptions must contain.[30] Since the court below concluded that ERISA's provisions do not preempt, but rather complement, the disclosure requirements of the securities laws[31] (App. 42), and because the antifraud

[30] Additional extensive reporting and disclosure requirements are provided for by ERISA. *See, e.g.*, §§102, 103, 104, 105, and 106.

[31] In this conclusion, the court below clearly misunderstood the significance of the Welfare and Pension Plan Disclosure Act of 1958 and ERISA to the issues raised in this case. Their significance does not lie in literal notions of implicit or express preemption, (App. 42-48), but rather in the fact that their legislative histories clearly demonstrate Congress' belief

provisions' affirmative obligations to disclose all "material" information are unquestionably broader than ERISA's, the securities law's antifraud disclosure provisions necessarily subsume ERISA's requirements *vis a vis* disclosure to plan participants. Thus, ERISA's provisions become superfluous and the question of disclosure to participants reduces itself to little more than one of timing. Since disclosure under the securities laws is to be made prior to the occurrence of a "sale" to facilitate the making of an informed investment decision, the holding below that the "sale" occurs, *inter alia,* when an employee decides to accept a job tacitly reverses Congress' determination that adequate protection is provided by disclosure within 90 days *after* the employee becomes a plan participant. 29 U.S.C. §1024(b)(1)(A). Significantly, an employee may not even become a participant for as much as one year from the date of initial employment. *Compare* 29 U.S.C. §1002(7) with §§ 1052(a)(1)(A)(i) and (ii).[32]

By affording a legal remedy to past plan participants who have failed to meet the eligibility requirements of their plans, the court below effectively reverses another Congressional policy determination manifested in ERISA. Any retroactive grant of pension benefits, either directly or disguised in the form of damages[33] for breach of the antifraud provisions, would clearly

that it was filling a regulatory void based, at least in part, on its perception that the securities laws did not apply to the employees' participation in the pension plan. *See, e.g.,* S. Rep. No. 1440, 85th Cong., 2d Sess. *reprinted in* [1958] U.S. CODE CONG. & AD. NEWS 4137, 4145, 4153, 4156; H.R. Rep. 2283, 85th Cong., 2d Sess. *reprinted in* [1958] U.S. CODE CONG. & AD. NEWS 4181, 4183; H.R. Rep. 93-533, 93d Cong., 2d Sess. 3-5, 7-11 *reprinted in* [1974]U.S. CODE CONG. & AD. NEWS 4639, 4641-3, 4645-9; S. Rep. No. 93-127, 93d Cong., 2d Sess. 3-8 *reprinted in* [1974]U.S. CODE CONG. & AD. NEWS 4838, 4840-4, 4847.

[32]The lower court concluded that "there is no provision of Title I [of ERISA] which generally prohibits the making of false or misleading representations to an employee concerning the pension fund." App. 46, n. 57. Any suggestion, however, that a plan administrator may lie to plan participants is totally specious. *See, e.g.,* 29 U.S.C. §§ 1021, 1022, 1131-33.

[33] The standard measure of damages under the securities laws is the difference between the fair value of that received and the fair value of what

contravene § 203(b)(1)(f) of ERISA (29 U.S.C. § 1053(b)(1)(f)) which expressly allows plans to disregard pre-ERISA years of service "which would have been disregarded under the rules of the pension plan with regard to breaks in service, as in effect on the applicable date." In other words, Congress' determination that pre-ERISA unvested liabilities need not be funded is neutralized by the decision below.

Additionally, the amorphous nature of disclosure under the antifraud provisions of the securities laws gives rise to widespread uncertainty with regard to the manner and timing of disclosure. It is clear that these provisions impose an affirmative obligation to disclose all "material" information. *Affiliated UTE Citizens* v. *United States,* 406 U.S. 128, 153 (1972). But the materiality of specific facts is determined on a case-by-case basis, *see, e.g., SEC v. Shapiro,* 494 F.2d 1301, 1306 (2d Cir. 1974), against a legal standard, *see generally TSC Industries, Inc., v. Northway, Inc.,* 426 U.S. 438 (1976), the meaning of which will raise more questions in the minds of those unaccustomed to dealing with the securities law than it answers. For example, the "risks" to which the ultimate realization of benefits are exposed reach far beyond the investment success or failure of the trust fund itself. An employee may never realize benefits from the plan because, *inter alia,* of death, early resignation, lay-off, protracted strike, or the inability of the employer to continue making contributions. Must each circumstance which has a possible bearing on the likely occur-

would have been received absent the fraudulent conduct. *Affiliated UTE Citizens v. United States,* 406 U.S. 128, 155 (1972). Thus, where benefits are totally forfeited the damages recoverable would appear to be the payment of full benefits or, at the very least, the sum total of contributions made by the employer on the employee's behalf, assuming such is determinable. However, because the decision below necessarily suggests that employment decisions are made on the basis of fringe benefits, liability in the form of consequential damages for such things as lost job opportunities and moving expenses incurred to accept a pension plan induced job may also attach. *See generally* A. Jacobs, *The Measure of Damages In Rule 10b-5 Cases,* 65 Geo. L.J. 1093 (1977). Such a result underscores the patent inapplicability of security law principles in the pension plan context.

rence of one or all of these events be disclosed? Does it make a difference that some of these "risks" involve circumstances exclusively within the employee's control? The decision below requires that such questions now be asked and properly answered under pain of massive antifraud liability.[34]

Once one determines what must be disclosed, the form and timing of disclosure again become critical. To be sure, those potentially liable cannot rely on oral disclosures given the liability which may result several years hence. Rather, detailed disclosure documents will have to be prepared and distributed to present and potential employees and other disclosures closely monitored, all at great cost to the pension trust funds and to the other parties. Further, because the court concluded that the operative "sale" normally takes place "when an employee decides . . . to continue employment in a job" (App. 48), employers, unions, and/or trust administrators must now gaze into the future to determine when an employee is about to decide not to continue in his job so that proper disclosures can be made *before* the "sale" is complete. Surely Congress could not have intended to impose such absurd burdens.

For employers whose retirement plans are collectively bargained, the problems of complying with largely undefined antifraud disclosure requirements are exacerbated by certain legal limitations inherent in the collective bargaining process. The decision below now leaves such employers with a "Hobson's Choice". Because of their potential liability under the securi-

[34] While the types of disclosure which will now have to be made are less than clear, the complaint herein provides a useful guide with regard to what the reasonable employee *qua* investor might consider "material". According to Mr. Daniel, and the lower court as well, the actuarial assumptions upon which the pension plan was based and the actuarial likelihood that he would ever realize his benefits should have been disclosed. But, as their names imply, such data are nothing more than assumptions based in part on the past experiences of group populations. As such they tell little or nothing with regard to what the experience of a specific individual will be, particularly when that individual alone controls many of the variables. Thus, to a large extent disclosure of such data may in and of itself be inherently misleading. Under the decision below, disclosure of such information will be required nonetheless.

ties laws[35], they can ill afford to sit back and rely on the accuracy of representations made by the union to its members concerning the bargained pension plan. Rather, prudence will dictate that employer representatives be present whenever the union makes any assertions concerning the plan to its members, and that they actively intervene to correct any false impressions suggested. However, any such action exposes the employer to potential liability under the National Labor Relations Act for interfering with internal union processes and undermining the union's status as the exclusive employee representative. *See, e.g.*, §8(a)(2) of the National Labor Relations Act (29 U.S.C. §158(a)(2); *NLRB v. General Electric Co.*, 418 F.2d 736 (2d Cir. 1969), *cert. denied*, 397 U.S. 965 (1970). Unionized employers are thus placed in the untenable position of facing liability under the securities laws for inaction, and liability under the labor laws for action. While such a choice might otherwise cause an employer to simply discontinue its plans, or at least reduce benefits to help compensate for disclosure costs, the unionized employer is further restricted because such matters are mandatory subjects of bargaining, *Inland Steel Co. v. NLRB,* 170 F.2d 247 (8th Cir. 1948), *cert. denied*, 336 U.S. 960 (1949), with regard to which the employer can make no unilateral changes. *See generally Fibreboard Products Corp. v. NLRB,* 379 U.S. 203 (1964).

Those who will bear perhaps the greatest burden of the decision below are past, present, and future pension plan participants. The costs of this decision will seriously undermine the financial viability of many pension funds. Indeed, a startling number of pension plans have already terminated as a result of the burdensome requirements imposed by ERISA.[36] Recogniz-

[35] The question of employer liability was specifically avoided by the court below (App. 50). However, there are legal theories which, under the facts of a specific case, may give rise to such culpability. *See, e.g.*, SEC Securities Act Release No. 5226 (1972) *reprinted in* [1977] Fed. Sec. L. Rep. (CCH) ¶2785; Mundheim and Henderson at 813.

[36] Of the relatively limited number of plans covered by the Pension Benefits Guarantee Corporation (*see generally* 29 U.S.C. §1321) roughly 7,300

ing that employers are under no legal obligation to provide retirement programs, and also that viable alternatives exist which eliminate the employer's involvement and leave the employees more or less to their own devices, the impact of a decision such as that below will, at the very least, discourage the establishment of new retirement plans, and could conceivably toll the end of the nation's voluntary private retirement system altogether. Nothing could be more antithetical to common sense and sound public policy.

CONCLUSION

For the foregoing reasons, and for the reasons set forth by Petitioners, this Court is respectfully requested to grant the Petitions for a Writ of Certiorari.

Respectfully submitted,

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single employer plans, an increase of sixty-five percent over 1975, terminated in 1976 alone. Analysis of Single Employer Defined Benefit Plan Terminations, Publication No. PBGC 505, at 1-2 (1976). Thirty-five percent of these terminations were reported as having been caused at least in part by ERISA. *Id.* With regard to multi-employer plans, recent data show that two percent of all such plans, covering roughly five percent of all participants in such plans, are affected by extreme financial hardship such that a high potential for plan termination within the next five years is indicated. 196 Daily Lab. Rep. (BNA) A-3 to A-4 (October 7, 1977). An additional ten percent of such plans covering fifteen percent of all the participants therein are having significant financial difficulties and show a potential for termination although not necessarily within the next five years. Id.